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C O N F I D E N T I A L SECTION 01 OF 04 SHENYANG 000173

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SUBJECT: LIAONING'S ECONOMY: DOWN BUT NOT OUT

Classified By: CONSUL GENERAL STEPHEN B. WICKMAN; REASONS 1.4 (b/d).

¶1. (C) Summary. Local leaders in three of the Liaoning Province's less well-off urban areas put a good front on this province's relative resiliency in the face of recession but privately conceded their worries. The most telling statistic is electricity demand, which was flat in October and dropped 11 percent in November, showing that manufacturing is clearly in recession. One Deputy Mayor said it was very unlikely that China's provinces would be able to meet the local stimulus targets set by Beijing unless the center provided additional funding. Meanwhile, Liaoning governor Chen Zhengao has taken a team of mayors and vice mayors on a mission to Guangzhou to help nearly bankrupt Guangzhou enterprises relocate or invest in Liaoning at bargain prices. End Summary.

¶2. (U) The Consul General and two local assistants paid first visits to two of Liaoning Province's poorest cities -- Fuxin and Chaoyang -- October 28-November 1 and to nearby Tieling, November 20-21. Joined by the Principal Commercial Officer and her staff for the Chaoyang segment, the visit to Western Liaoning was heavy on commercial content. The schedule also included a speech at the Liaoning Engineering and Technology University -- to our knowledge, the first ever outreach event at this venue -- and a heartwarming stop at a school for orphans -- one of only two such schools in the country (the other is in Jilin Province). The Tieling visit featured a visit to the "new city" development project, which will open this month.

King Coal in Fuxin...

¶3. (SBU) It's been a long time since anyone from the consulate visited Fuxin, one of the poorest of Liaoning Province's fourteen municipalities, but it's a lot easier now that we can fly along the province's newest expressway (opened in late September). The signage is so new that our Foreign Affairs Office (FAO) handlers could not tell us where to turn off, but Fuxin is working hard to take advantage of the new link. Among our discoveries: Fuxin has one of the best-run government-owned guest houses in these parts; hosts a renowned international Agate Festival; is the "Basketball Capital" of the northeast; and is dominated by state-owned power companies expanding aggressively toward Inner Mongolia. Fuxin has also just established a sister-city relationship with Gary, Indiana and hopes for more cooperation with U.S. and other foreign enterprises.

¶4. (SBU) Mayor Pan Liguogave the usual virtuoso recap of Fuxin history, especially its 60-year record as a coal-mining and power-production center, noting that reserves are nearly exhausted. At the current extraction rate -- around 20 million tons per year -- Fuxin's reserves will

last only another 20 years. The 35,000 miners currently employed at state-owned facilities are down from a peak of 200,000, and there are now only 30,000 miners working in private mines. The city is trying to develop substitutes: coal-mine gas, wind turbines, and coal-based chemicals linked to Inner Mongolia's Xilin Gol Area, whose rich reserves may reach 200 billion tons. In 2007, the National Railway Corporation began construction to link Fuxin and the Xilin Gol area. A coal gasification project with an investment of RMB 26.4 billion (USD 3.86 billion) has received the National Development and Reform Commission's first-stage approval and is in the final "assessment" period. The development will more than fill Liaoning's annual gap in demand for coal and products of around 800,000 tons per year. Fuxin is also building the country's largest wind power plant, located next to the Kerqin Grasslands of Inner Mongolia, which will have 600 megawatts of installed capacity by year end, about a third of the final target. The mayor was sanguine about the real estate industry, reporting that prices are continuing to rise even for "economic" housing to replace the old slums.

15. (SBU) Liaoning Engineering and Technology University (LETU) Vice President Wang Jiren, an expert on mine safety, told us that 100 percent of China's current coal mine accidents are caused by "human error" stemming from a lack of strict management controls and poor education. Wang said there is an unflattering saying that "one only becomes a miner if one can do nothing else and has no other choice." So the key to increased safety -- and Fuxin has had its share of disasters -- is how to educate the miners and improve their quality. Wang added

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that small-scale mine owners are especially reluctant to invest in safety facilities, another reason for the high frequency of accidents. Wang reported that Liaoning has "begun" to close all its private mines (about 100 in all) and prohibits owners from becoming involved in production and management; they simply own shares and receive dividends. Each private coal mine will be assigned a qualified mining management company.

16. (U) During a brief visit to a coal-mine-gas generating station run by Fuxin Mining Group, Deputy Chief Engineer Wei Huaxing told us the group had built 47 such generators at different pumping stations. Total capacity has reached 24,600 kilowatts --one quarter of group's in-house needs. The pumping stations use the existing coal-mine gas emission wells, which used to let the gas into the air, causing pollution and waste. Wei reported that gas having a density of over 30 percent can be used directly for combustion engines while a density of 10 percent can be converted easily to power. Density inside the mines must be limited to 0.5-0.7 percent to prevent explosions, which occur at levels exceeding 0.75 percent. The group is researching the utilization of even these very low densities. Wei also noted that Fuxin Mining Group cooperates with Japan on a gas purification project and receives pollution offset subsidies through the UN programs. The site we visited had a 10,000-cubic-meter storage tank, which Wei said they would tap when prices spiked. On the road, for example, we passed a crowded queue at one of the city's two coal-mine gas stations for converted taxis, which have proven extremely popular with local drivers. Fuxin Mining Group and the state-owned gasoline companies helped re-equip the taxis at a cost of only RMB 200 (USD 30) per engine so that the taxis can use either coal gas or gasoline through the flip of a simple switch. The coal gas is only one third of the price of gasoline.

...Burns Less Brightly for Now

17. (C) Over lunch, Deputy Mayor Zhang Bengang went into an

animated critique of the NDRC approval system, which was the biggest obstacle to getting things done at the local government level. He said getting NDRC approval was more difficult than for any of the line ministries required for project development and that the system was non-transparent and slow. Over breakfast, Zhang continued critiquing the growing number of unfunded mandates being dictated by the central government, a theme that he returned to during a Thanksgiving event held on November 30 in Shenyang. Zhang said that the stimulus package enacted by the central government in response to the global economic recession required each province to achieve unrealistic expenditure targets that had to be financed locally. He said that relatively prosperous provinces like Liaoning might come close to meeting their targets but that poorer provinces in the South and West would never be able to meet the mandates without additional central government funding. Zhang had praise for Liaoning governor Chen Zhengao, who he was joining on a mission to Guangzhou the following day. Chen's mission was to entice nearly bankrupt Guangzhou enterprises to relocate or invest in Liaoning. Chen planned to offer old factories and land at bargain prices in an effort to both save the southern enterprises and expand employment in Liaoning.

Chaoyang's Fossil Imagination

18. (SBU) Chaoyang Deputy Mayor Chen Lie described his administration of over 20,000 square kilometers, Liaoning's largest district in terms of area and fourth largest in terms of population (3.7 million). Covering five counties, two county-level cities, two districts, and one provincial-level development zone, Chaoyang remains the least-developed area in Liaoning, though the growth rate in local GDP and government revenue skyrocketed to first place in 2007. Chen predicted another leap in GDP this year, from RMB 33.4 billion in 2007 to RMB 43 billion, while government revenues climb from RMB 2.2 billion to RMB 3 billion. Chaoyang has seen a big increase in fixed asset investment, especially as reflected in the expansion of Lingyuan Iron and Steel, a joint venture with Anshan Steel. By the time expansion is completed in 2010, Chaoyang will have an annual steel capacity of 10 million tons.

19. (SBU) Chaoyang Mayor Zhang Tiemin boasted about the

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city's world-class fossil museum that has hosted two international conferences on paleontology and that will soon double in size (replete with golf courses for an expected up tick in Japanese and Korean visitors) and the construction of a new museum downtown. Despite the area's relative poverty, the rate of college enrollment is high (third highest in Liaoning) and the government provides generous assistance to the poor through direct financial subsidies, vocational training, and farming aid. He said the average net income for a farmer in Chaoyang is now about RMB 4,300 (USD 630) per year. Asked about the effects of the international economic downturn, Zhang mentioned that the Feima Group's exports of tires and hubcaps to North America had fallen off substantially but he was otherwise sanguine. He similarly shrugged off the fact that his district was the only district in the province to suffer a net decline in agricultural production this harvest year, saying that the peasants expected this to happen one out of every four or five years. He also remarked on the growing relationship between Navistar International (a U.S. firm) and state-owned Dongfeng Chaoyang Diesel.

110. (C) Note: Tieling Vice Mayor Zhou Yiyang contradicted both Mayor's accounts when we met with her at lunch in Tieling on November 20. She said the mayor had complained to her that reduced demand was seriously affecting the

steel and mining industries in Chaoyang and she did not expect Chaoyang to reach its targets. (Zhou's staff toasted her repeatedly at lunch about her recent "election" to the Standing Committee of the Tieling Communist Party Committee. Zhou, who speaks almost fluent English, received an MBA at Chicago's Roosevelt University and is clearly an up-and-comer in this province.)

A Peek at Chaoyang's Welfare Institutions

¶11. (SBU) Chaoyang's earthy Director of the Civil Affairs Bureau (also the Director of the Chaoyang Charity Federation) took the CG on a tour of one section of the Chaoyang Municipal Welfare Institute, which consists of a Children's Center and Senior Citizens Home. The director of the children's facility said there were currently some 40 abandoned children and orphans, most of whom had severe physical or mental disabilities. The orphanage works with two U.S.-based charities, AWA or the American International Adoption Center, to sponsor annual visits to the children for one to two weeks at a time, helping the children with rehabilitation. One other U.S.-based medical organization also has a relationship with the facility. About 20 children have been adopted overseas. Compared to the Shenyang facility we have visited, this facility was clearly understaffed and the rehabilitation equipment hardly used.

¶12. (U) By contrast, the Liaoning Provincial Orphans School in Chaoyang appears to be a stunning success that dates from the Cultural Revolution (the school was established in 1965). One of only two such institutions in China (the other is in Jilin Province), the school combines nine years of compulsory education with vocational training to help abandoned or orphaned children succeed in mainstream society. The vocational school, for example, trains students in computer accounting, computer application and maintenance, preschool teaching, fashion design and tailoring, cooking, beauty and hair styling, and other vocations and boasts a perfect placement rate. Recently, the middle school reports a 100-percent success rate in placing its graduates in high school or vocational school, of which another 80 percent make it into college, including many in graduate programs. All the students board on campus, some 6-8 students per room with a resident teacher to insure care outside of the classroom. All of the financing comes from the provincial government and the Liaoning Charity Federation, and the children come from 14 cities all over the province. U.S. NGOs, including the Casey Cares and Half the Sky Foundations have worked with the school in the past, but only a dozen or so children aged 8-10 have been adopted overseas.

¶13. (U) The school's dynamic principal, Tong Zixinm, told us he has worked in the school for 14 years and spends every spring Festival with the children: "It's like a big family." Tong had been a Youth League Secretary at Chaoyang Teachers College before transferring. Since then, the number of students has more than tripled to the current level of 648 and Tong proudly looked forward to being able to handle over 1,000 students in the large, new facility

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which opens in Shenyang in 2010. The school has had 3,000 graduates overall since its founding.

Tieling's Gleaming Aluminum Future

¶14. (C) Tieling Mayor Zhang Jiangqiang was extremely upbeat about his successful trip to the United States last spring when he visited Alcoa headquarters in Pittsburgh and signed contracts with five U.S. and Canadian investors, including Alcoa. He stressed that Tieling will not be affected by the global economic crisis because the city has

few export-oriented factories and relies instead on producing lathes and mining machinery. Despite the downturn, moreover, Alcoa confirmed that it will follow through on its plan to build an aluminum fixture fabrication plant in Tieling even though Alcoa decided to scrap a similar plant in Eastern Europe. Zhang admitted, however, that electricity demand had dropped 11 percent in November province-wide, proving there was indeed a recession in manufacturing. (Note: When he was Party Secretary of Liaoning Province, Vice Premier Li Keqiang told the Ambassador that electricity production was one of only two consistently reliable indicators of economic activity in China; the other was bank credit.)

15. (SBU) Tieling's "New Town" is being built with aluminum fittings that will eventually be produced in Alcoa's planned factory in the industrial zone. Located 4.5 kilometers south of the old city, the new town will hopefully propel real estate development in a city that has seen its share of economic woes. Prices for housing in the new town have actually risen over the past few months. The government will formally move to its new headquarters on the banks of a man-made lake sometime in December. One of the features of the new government headquarters appears particularly apt, if not unique: the government building is flanked by the local People's Congress, on the right, and the Political Consultative Committee, on the left, and the central office structure is split evenly down the middle between the city government and the communist party offices. Communication should be excellent.
SWICKMAN